No. 95-244

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

CHUCK QUACKENBUSH, INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, IN HIS CAPACITY AS LIQUIDATOR AND TRUSTEE OF THE MISSION INSURANCE COMPANY TRUST, MISSION NATIONAL INSURANCE COMPANY TRUST, ENTERPRISE INSURANCE COMPANY TRUST, HOLLAND-AMERICA INSURANCE COMPANY TRUST AND MISSION REINSURANCE CORPORATION TRUST,
Petitioner,

v.

ALLSTATE INSURANCE COMPANY,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONER

I. INTRODUCTION

The Commissioner's Opening Brief adequately addresses most of the points discussed in the Briefs of Allstate and the *Amici Curiae*. This Reply Brief For The Petitioner primarily focuses on several new issues introduced by Allstate and its *Amici*.[1]

This Court granted Certiorari on two issues. In violation of this Court's Rule 14.1(a), however, Allstate has attempted to restate and change the substance of the second issue before this Court.

The opinion of the Ninth Circuit was succinctly limited:

> This case presents two questions: First, whether a remand order based on abstention is reviewable, and, if so, whether it can be reviewed on appeal, or only by a petition for a writ of mandamus. Second, and more importantly, we consider whether the Burford abstention doctrine allows a federal court to surrender jurisdiction to a state court in a case in which no equitable relief is sought.

Pet. App. p. 2a. Further, the Ninth Circuit specifically stated that it did not reach the question of whether this case met the requirements for abstention under *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943). Pet. App. p. 8a n.8.

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[1] In his Opening Brief, p. 5 n.13, the Commissioner referred to a then-pending appeal before the California Court of Appeal, *Imperial Casualty & Indemnity Co. v. Insurance Commissioner of the State of California*, case number B083725. In December 1995, that case was decided in the Commissioner's favor. *In re Mission Insurance Company (Imperial Casualty)*, 48 Cal. Rptr. 2d 209 (1995). The primary basis of that opinion rested on the specific provisions of a settlement agreement between the Commissioner and Imperial. Thus, that particular open dispute is resolved. However, other disputes concerning the proper application of *Prudential Reinsurance Co. v. Superior Court (Garamendi)*, 3 Cal. 4th 1118, 842 P.2d 48, 14 Cal. Rptr. 2d 749 (1992), and California Ins. Code § 1031 remain open.

The second issue upon which this Court granted Certiorari is:

> Whether the court below erred in holding that the abstention powers of federal courts are limited to actions in equity, or alternatively, whether that court erred in limiting the exercise of *Burford* abstention solely to actions in equity.

Although under this Court's rules, an issue fairly included within the issues before the Court may be raised, Allstate seeks to change the focus of the second issue by suggesting this case is not "public" and is no more than an ordinary damage suit against a private party. Allstate's version of the second issue is:

> Whether an action at law against a private party seeking money damages can present the exceptional circumstances necessary for a federal court to decline to exercise its jurisdiction based on the *Burford* doctrine.

Brief for Respondent, p. (i).

Thus, Allstate attempts to alter the question before the Court from one involving the fundamental power and discretion of the federal district court to abstain in any case *"at law"* to a dispute over whether the *Burford* abstention doctrine may apply to a damage case involving private parties.[2] This effort to transform the issue is inappropriate and for the reasons discussed below, Allstate (with the support of its *Amici, see, e.g.*, Brief of Nat'l Ass'n of Indep. Insurers, et al., at p. 14) cannot successfully characterize *either* the Commissioner or Allstate as merely private parties in the context of this case.

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[2] Even this different issue is not an open one because this Court has already applied abstention doctrines to actions between "private" parties. For example, *Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100 (1981), involved private plaintiffs seeking actual and punitive damages against tax officials in their "private" capacities. *See also Kaiser Steel Corp. v. W. S. Ranch Co.*, 391 U.S. 593 (1968).

II. RESPONSE TO ALLSTATE'S ARGUMENT THAT THE REMAND ORDER WAS REVIEWABLE BY APPEAL

At page 10 of its Brief, Allstate enunciates the crux of its argument on the first issue as follows:

> A remand based on the *Burford* doctrine satisfies the most basic principles of finality because it ends the litigation in the district court and leaves that court with nothing further to do. Because the remand order here put Allstate "effectively out of federal court"—indeed, put Allstate expressly and literally out of federal court—it was final and appealable under Sec. 1291.

Allstate's assumption that it is "effectively out of federal court" is not necessarily true. Moreover, this case began in *state* court and, under the remand order, the *same* case would proceed in the *same* state court. Allstate's wish to be in an arbitration proceeding, rather than federal or state court, may or may not be granted by the state court. If the proceedings in the state court eventually deny some federal right to arbitrate, then Allstate may seek to adjudicate in federal court such federal questions as may then exist. Indeed, since Allstate claims the right to arbitrate under a contract provision, it is possible Allstate may assert a federal law issue under the Federal Arbitration Act and/or the Contract Clause of the Constitution. Those issues are not yet ripe, however, since they depend on antecedent issues of uncertain state law, and Allstate cannot show it is "effectively out of federal court." To be sure, Allstate's desire to have a federal court rule on the issue of arbitrability may be delayed, but it may also become moot.[3] Assuming *arguendo*, that it

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[3] Allstate's alleged right to arbitrate is an open and complex issue under both state and federal law. *See, e.g., Corcoran v. Ardra Ins. Co., Ltd.*, 657 F. Supp. 1223 (S.D.N.Y. 1987); *Doughty v. Underwriters at Lloyd's, London*, 6 F.3d 856 (1st Cir. 1993). Indeed, the antecedent state law issue and its uncertainty are effectively acknowledged in the *amicus* brief of the Reinsurance Ass'n, et al. at p. 23 n.20. Allstate argues that it is irrelevant that the issue is undecided under state law, but the fact that an alleged federal question, par-

does not become moot, but is merely delayed, that delay is insufficient to render the remand order appealable. *See, e.g., Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336 (1976); *Lauro Lines s.r.l. v. Chasser*, 490 U.S. 495 (1989); Commissioner's Opening Brief, pp. 26-27.

In *Thermtron*, this Court squarely held that "an order remanding a removed action does not represent a final judgment reviewable by appeal," but only (in a proper case) by mandamus. 423 U.S. at 352. In *Things Remembered, Inc. v. Petrarca*, 516 U.S. ——, 116 S. Ct. 494, 496 (1995), this Court recently confirmed its position in *Thermtron* that only those remand orders within 28 U.S.C. § 1447(c) are barred from appellate review under 28 U.S.C. § 1447(d). However, the Court also noted that "Congress has placed broad restrictions on the power of federal appellate courts to review district court orders remanding removed cases to state court."[4] Further, the Court did not hold that all remand orders not barred by 28 U.S.C. § 1447(d) *are* appealable; nor did it retract *Thermtron's* rule that a remand order is not a final appealable judgment and may be reviewed only by mandamus.

ticularly a Constitutional law issue, might be mooted in the pending state court litigation is certainly one of the factors, among others, that a district court may consider in determining whether or not to abstain. *See, e.g., Railroad Comm'n v. Pullman*, 312 U.S. 496 (1941). Further, though not necessarily controlling, it is at least pertinent to note that Allstate did not (and could not) remove on the basis of a federal question, but rather on the basis of diversity of citizenship . . . a basis that existed only because of the fortuity that the Commissioner, instead of the state agency itself, is designated as liquidator and trustee by state law.

[4] *See also Things Remembered*, 116 S. Ct. at 500 (Ginsburg, J., concurring: "In sum, a 'strong congressional policy against review of remand orders' . . . underlies Sections 1447(d) and 1452(b)" (citing, *inter alia, Sykes v. Texas Air Corp.*, 834 F.2d 488 (5th Cir. 1987) ("The [analysis suggested to that court] turns on a sort of semantic crack in the statute rather than a sound appreciation of the strong congressional policy against review of remand orders.").)

Unless the Court were now to hold that all remand orders *are* final orders, remand orders should not normally be reviewable by appeal. The exception, if any, to this general rule would be the collateral order doctrine established in *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949). If this remand order qualifies under *Cohen*, then all remand orders not appeal-barred by Section 1447(d) could be appealed.[5] The result would be to increase the number of appeals in the federal system, perhaps by several thousand cases a year,[6] and significantly broaden the "narrow exception" the Court recognized in *Cohen*. Whether or not any remand order could ever qualify under the *Cohen* exception, this one does not.

III. RESPONSE TO ALLSTATE'S ARGUMENT REGARDING THE PROPRIETY OF ABSTENTION

The effect of the Ninth Circuit decision is that a district court may *never* abstain unless the underlying pleading asserts a case "in equity" within the meaning of the ancient distinction between law and equity. Although the Ninth Circuit specifically referred to *Burford* abstention, its rationale is far broader and rests on the concept that a district court may not abstain except as a matter of the

[5] The Commissioner believes it would be better to view all remand orders as within the bar of Section 1447(d) and by no means concedes the opposite. *See* Commissioner's Opening Brief, pp. 29-30, and n.52. The Commissioner is aware that *Thermtron* holds otherwise, in the context of its particular facts, but as stated in a concurring opinion in *Things Remembered*, the applicability of the *Thermtron* exception in other contexts (such as this), remains open. *See* 116 S.Ct. at 498 (Kennedy, J., concurring). *See also* Joan Steinman, *Removal, Remand and Review in Pendent Claim and Pendent Party Cases*, 41 Vand. L. Rev. 923, 1004 (1988), distinguishing *Thermtron* from discretionary remand orders). To the extent that holding is found to be in issue in this case, the Commissioner wishes to make his position clear.

[6] Michael E. Solimine, *Removal, Remands and Reforming Federal Appellate Review*, 58 Mo. L. Rev. 287, 289 (1993).

court's "discretion to decline or grant equitable relief." Pet. App. p. 10a.

The utter inflexibility of the Ninth Circuit rule is completely at odds with the nature and purpose of the abstention doctrine. The Commissioner *agrees* with the Ninth Circuit that, in order to abstain, a district court must exercise its "discretion to decline or grant equitable relief." Pre-merger, a district court arguably could grant equitable relief only when it sat in equity as a result of the underlying suit being "in equity." However, under the merged federal system, a district court that has jurisdiction *always* sits in both law and equity.

The granting of the Commissioner's motion seeking remand of this case *was* the exercise of the district court's discretion to grant equitable relief. Under modern procedure, the propriety of a district court's exercise of its equity powers depends on the circumstances of the particular case before it. To etch upon abstention principles an arbitrary and outdated rule that *must* be applied in all cases for all time, regardless of individual circumstances, would be an abdication of the important judicial duty to protect "Our Federalism." This duty deserves the same degree of fealty as a court's general obligation to exercise its jurisdiction.

Allstate never even attempts to distinguish this Court's statement in *Louisiana Power & Light Co. v. Thibodaux*, 360 U.S. 25, 28 (1959), that:

> These prior cases have been cases in equity, but they did not apply a technical rule of equity procedure. They reflect a deeper policy derived from our federalism. We have drawn upon the judicial discretion of the chancellor to decline jurisdiction over a part or all of a case brought before him.

Further, Allstate has not explained why the district court in this case was not "sitting in equity" when it remanded this case, given current federal rules of civil

procedure; particularly Federal Rule 2 and this Court's holding in *Ross v. Bernhard*, 396 U.S. 531 (1970).[7]

Instead, Allstate apparently advances the novel concept that the Commissioner is not really a public official in the context of this case and that this is an *in personam* suit to establish a debt between private parties. This position avoids the fundamental question presented in the Petition for Certiorari, and as shown in Part A below, it is also wrong.

A. This Is Not an Ordinary *In Personam* Action Against a Private Party

It is well-settled that insurance is a public asset and a business which affects the vital public interest. Contracts of insurance and reinsurance have greater public consequence than contracts between individuals to do or not to do a particular thing whose effect stops with the individuals. *See, e.g., German Alliance Ins. Co. v. Lewis*, 233 U.S. 389, 413 (1914); *Nebbia v. New York*, 291 U.S. 502, 523 (1934); *Osborn v. Ozlin*, 310 U.S. 53, 65 (1940); *California State Auto. Ass'n Inter-Ins. Bureau v. Maloney*, 341 U.S. 105, 109 (1951).

The law is clear that the Commissioner acts in his official capacity as an officer of the state in connection with the underlying proceedings. Cal. Ins. Code §§ 1011, 1059; *20th Century Ins. Co. v. Garamendi*, 8 Cal. 4th 216, 240, 878 P.2d 566, 580, 32 Cal. Rptr. 2d 807, 821 (1994), *cert. denied*, 513 U.S. ——, 115 S. Ct. 1106 (1995); *Carpenter v. Pacific Mut. Life Ins. Co.*, 10 Cal. 2d 307, 329, 74 P.2d 761, 774-75 (1937), *aff'd sub nom. Neblett v. Carpenter*, 305 U.S. 297 (1938).

In the present context, neither the Commissioner *nor* Allstate may be viewed simply as a "private individual." It may be true that Allstate enters into a private contract

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[7] *See also* Commissioner's Opening Brief, pp. 19, 33-35, and see *Things Remembered*, 116 S.Ct. at 498-99 (Ginsburg, J., concurring, emphasing the significance of merger in the context of references to "equitable" grounds.).

when it purchases a company car, or contracts for its paper and pencils, but Allstate enters into publicly regulated and controlled contracts when it issues insurance policies or assumes reinsurance obligations. *Carpenter v. Pacific Mut. Life Ins. Co.*, 10 Cal. 2d at 329, 74 P.2d at 775 ("Insurance is a public asset, a basis of credit, and a vital factor in business activity."); *Garamendi v. Executive Life Ins. Co. (Morgan Stanley Mortgage Capital, Inc.)*, 17 Cal. App. 4th 504, 515, 21 Cal. Rptr. 2d 578, 585 (1993) ("The interest of a particular individual policyholder aside, insurance is a public asset and the public has an important stake in preserving the business.").

Indeed, all relevant insurance law of California is deemed to be a part of all of Allstate's insurance and reinsurance contracts, including its agreements with the Mission Companies. *See Alpha Beta Food Mkts., Inc. v. Retail Clerk's Union*, 45 Cal. 2d 764, 771, 291 P.2d 433, 437 (1955); *Hal Roach Studios, Inc. v. Richard Feiner & Co.*, 896 F.2d 1542, 1548 (9th Cir. 1989).

The background of the underlying proceedings is detailed in the Commissioner's Opening Brief, pp. 2-16, a discussion that Allstate does not materially dispute.[8]

[8] Allstate disputes that the downfall of the Mission Companies was the fault of the reinsurers and in its Brief at p. 6 n.4 goes outside the record to cite to a highly political and incorrect document produced by the Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce entitled *Failed Promises: Insurance Company Insolvencies*, Committee Print 101-P. 101st Cong., 2d Sess. (1990). That document was produced after the most cursory of investigations which never actually focused upon the operations of the Mission Companies, but dealt with an affiliated general agency and the parent company, Mission Insurance Group, Inc. In the *amicus* brief of the Reinsurance Ass'n, et al. at p. 5 n.6, a similarly motivated reference is made to a tentative ruling of a panel acting under the auspices of the Receivership Court. But on December 28, 1995, the Receivership Court completely rejected this panel's tentative decision and refused to give it any effect, in the process referring to the decision as "comic." Apparently, Allstate and the *Amici* are attempting to suggest that the four separate Insurance Commissioners who have been in charge of these proceedings for almost 10 years have all acted incorrectly and have had no valid grounds to require a turnover of the Reinsurance Recoverables. However, the fact that several hundred very sophisticated reinsurers have paid over $1.2 Billion to the Commissioners speaks eloquently in support of the rectitude of the Commissioners' positions and against the suggestions of Allstate and the *Amici*.

Despite this, Allstate and its *amici* appear to argue that a suit by a state insurance commissioner, acting to marshal assets under a special proceeding in the exercise of California's police power is somehow converted to an *in personam* damage suit between private individuals. However, this Court recognized the insupportability of this premise in *United States v. Bank of New York & Trust Co.*, 296 U.S. 463, 477 (1936). The underlying action is a suit to marshal and liquidate assets and is intimately connected with the liquidation proceedings. And in *Bank of New York*, this Court squarely characterized state court receivership proceedings, including suits to marshal assets and liquidate estates, as *quasi in rem*.[9]

[9] *See also Farmer's Loan & Trust Co. v. Lake S.E.R. Co.*, 177 U.S. 51, 61 (1900) to the same effect. The Commissioner widely cited *Bank of New York* in his Opening Brief, and included an extensive quotation at p. 7 n.18, but Allstate had no answer other than to ignore it. *See also Checker Motors Corp. v. Superior Court*, 13 Cal. App. 4th 1007, 17 Cal. Rptr. 2d 618 (1993) where that court noted state law recognizes "California's strong interest in preserving the assets of its policyholders and the insolvency court's interest in maintaining control over all of the insolvent insurance company's assets. . . ." *Id.* at 102.

At the same time, Allstate and its *Amici* cite several inapposite cases to support their position. *See, e.g., amicus* Brief of the Reinsurance Ass'n, *et al.*, pp. 18-19. *Morris v. Jones*, 329 U.S. 545, 549 (1947) has a narrow holding on a completely different set of facts and supports the Commissioner's argument that the injunctions issued by the state court in this case are entitled to full faith and credit. *Coit Independence Joint Venture v. Federal Sav. & Loan Ins. Corp.*, 489 U.S. 561 (1989) is not on point. It merely held that the FSLIC did not have the power to usurp the power of the courts. *Markham v. Allen*, 326 U.S. 490 (1946) is not an abstention case, it merely held that the district court did have jurisdiction, a prerequisite to abstaining. *Commonwealth Trust Co. v. Bradford*, 297 U.S. 613 (1936) strongly supports the Com-

In *Morgan Stanley Mortgage Capital v. Insurance Comm'r,* 18 F.3d 790 (9th Cir. 1994), the Ninth Circuit made exactly such a ruling and, in the process, refuted the position that this is merely a private suit. That case involved the insolvency proceedings of Executive Life Insurance Company, the same California statutory scheme as the instant case and virtually the same state court orders and injunctions as those issued here which assumed sole and exclusive jurisdiction over all the insolvent insurer's assets and all suits or claims against those assets.

In *Morgan Stanley,* the Ninth Circuit held that the reach of the state receivership court's jurisdiction was broad enough to encompass the insolvent insurer's interests in certain underlying partnerships even though those entities were not insurance companies. *Id.* at 794. That court acknowledged the strong public policy involved in insurance receivership proceedings and held that the state receivership court must have jurisdiction equally as broad as the jurisdiction of bankruptcy courts. *Id.* at 794. Indeed, the Ninth Circuit relied, among other authorities, on the clear Congressional intent expressed by the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015 to defer to state insurance regulation.

Also, the Ninth Circuit cited, with approval, the related California Court of Appeal case of *Garamendi v. Executive Life Ins. Co. (Morgan Stanley Mortgage Capital, Inc.),* 17 Cal. App. 4th 504, 21 Cal. Rptr. 2d 578 (1993) where the court among other things, noted that the proper jurisdiction of disputes over the insolvent insurer's assets was in the receivership court, that the receivership court has broad power to issue injunctions to protect the insurer's assets, and that the public has an interest in the orderly liquidation of an insurer. *Executive Life,* 17 Cal. App. 4th at 515, 21 Cal. Rptr. 2d at 585.

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missioner because it states that the court did have jurisdiction which it should exercise unless "required by rules based on comity to relegate the complainant to state court." *Id.* at 602.

Allstate does not dispute the discussion in the Commissioner's Opening Brief as to the key public nature of the Reinsurance Recoverables (Commissioner's Opening Brief, pp. 8-17), which are carried on the books of insurers *as assets* of the reinsured company and are, thus, in essence, public assets. Allstate must be presumed to have known and intended that its reinsurance obligations would be deemed assets of the Mission Companies and would be relied upon by the public and the regulators in permitting the Mission Companies to continue to do business.[10]

It is certainly a matter of public concern when Allstate attempts to avoid its contractual obligations after permitting the public and the insurance regulators to rely upon the Reinsurance Recoverables as assets and to believe they were "in good hands with Allstate." [11]

Upon the insolvency of the Mission Companies, Allstate filed claims in the underlying state court insolvency proceedings. It withheld from the Commissioner, acting as a public official, the Reinsurance Recoverables which are in *custodia legis* of the state court, title to which

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[10] Allstate's reinsurance contracts with the Mission Companies include an "Insolvency Clause" which clearly contemplates that Allstate will be subject to the California insolvency statutes in the event of the insolvency of any of the Mission Companies. This clause, which is quoted in the Commissioner's Opening Brief, p. 49 n.93 (*see also, e.g.,* Jt. App. pp. 109-110), mandates, upon insolvency of the reinsured company, the payment of the reinsurance recoverables *without diminution* to the liquidator.

[11] The public and the State of California have a vital interest in these contracts. Much of the insurance in question was for large commercial risks and for workers compensation. There are hundreds of thousands of innocent individuals who are reliant upon the efficacy of the policies in question. These are not mere "private contracts" but are public contracts where individuals with severe workers compensation claims, with diseases from toxic shock, agent orange, breast implants, asbestos, PCP and various toxic environmental problems were made to rely upon the availability of the Reinsurance Recoverables from Allstate and the other reinsurers. Allstate and the Mission Companies operated under these contracts for over 17 years prior to this receivership.

was transferred to the Commissioner by operation of law, and sole and exclusive jurisdiction over which was assumed by valid orders of the Receivership Court.

In a further effort to assert that only private matters are at issue here, Allstate falsely claims that the funds needed to pay the covered claims of policyholders under the guaranty association statutes are private funds and come from the insurance companies that are members of the various guaranty associations. This is just not true. As was pointed out in the Commissioner's Opening Brief, p. 13 n.32, the ultimate source of these funds is not the insurance companies, but the public.[12]

In the face of the decision in *Morgan Stanley*, 18 F.3d 790, it is impossible to believe that the Ninth Circuit would have accepted Allstate's new argument that this dispute does not affect California's public interest had Allstate made this argument there. To make this argument now is not only to inject an inappropriate issue, but one that is wholly without merit.

B. The Administration of Abstention Doctrines Depends on a Reasoned Analysis, Not a Mechanical Checklist

Allstate engages, at pages 26-38 of its brief, in a highly technical and mechanical analysis of the *Burford* doctrine. In this effort, Allstate continues to attempt to shift the argument from the question at hand to an issue it would prefer to argue. Rather than confronting head-on the question of whether a district court *ever* has the power to abstain in a case "at law," Allstate expends a great deal of its effort in arguing why the district court should not have made the decision it made in this case.

Allstate's efforts to pigeonhole the abstention doctrines is not productive and only serves to confuse the issues. The abstention doctrines are not to be applied via a mechanical checklist; rather the courts are to conduct a careful balancing of the important factors as they apply in a given case. These factors are to be applied prag-

[12] *See, e.g.*, Cal. Ins. Code 1063.14.

matically with a view to the realities of the case at hand. *See Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 16 (1983) and *Law Enforcement Ins. Co. v. Corcoran*, 807 F.2d 38, 40 (2nd Cir. 1986), *cert. denied*, 481 U.S. 1017 (1987). The fundamental realities of the instant case are that the underlying dispute is firmly "entangled in a skein of state law," [13] and is an important and integral part of the insurance insolvency proceedings. These insolvency proceedings are special proceedings which entail various judicial actions and various administrative actions and determinations by the Commissioner.

In attempting to narrowly define a *Burford* pigeon-hole and write the Commissioner out of it, Allstate also sidesteps the fact that prior to this Court's decisions which gave rise to the *Pullman*, *Younger*, *Burford* and *Colorado River* abstention doctrines, it applied abstention-oriented principles in *Penn Gen. Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935), and in *Pennsylvania v. Williams*, 294 U.S. 176 (1935). The doctrine established there is uncomplicated. This Court held that a district court may properly relinquish its jurisdiction in favor of a state insolvency official where: i) there is a pending state court proceeding involving an insurance company or a building and loan company; ii) the end sought by that proceeding is the liquidation of a domestic insurance company or building and loan by a state officer; and iii) there is no showing that the interests of creditors and shareholders would not be protected by the state court. Allstate attempts to distinguish the instant case from *Penn General* and *Williams* by asserting that the underlying case is *in personam*. But as noted above, the underlying state proceeding is not *in personam*, it is *in rem* or *quasi in rem*. And even if it were considered in *personam*, that would make no difference. This Court and other courts have recognized that the marshaling of assets is crucial to an effective liquidation process. Thus, an interference with this vital process is

[13] *See McNeese v. Board of Education*, 373 U.S. 668, 674 (1963).

an interference with the underlying state court proceedings and with the associated administrative activities of the Commissioner as receiver.

Allstate also fails to face this Court's decision in *Moore v. Sims*, 442 U.S. 415, 428 (1970), where it was held:

> Few public interests have a higher claim on the discretion of a federal chancellor than the avoidance of needless friction with state policies, whether the policy relates to the enforcement of the criminal law (citations omitted) or the administration of a *specialized scheme for liquidating embarrassed business enterprises.* (emphasis added)

Significantly, in *Moore*, this Court cited *Pennsylvania v. Williams* in support of this proposition.

Fostering and protecting principles of federalism is vital to our system of government. This Court has never suggested that it would require district courts to implement federalism principles by rote deference to a simplistic litmus test, with judges never lifting their eyes to see and consider the particulars of the actual cases before them. On the contrary, this Court has guided and guarded the delicate balance of "Our Federalism" through the application of *reasoned discretion*, not an insensible application of an arbitrary and inflexible rule based upon irrelevant historical distinctions.

C. The Abstention Doctrine Should Not Depend on an Out-Dated Law/Equity Distinction

The core question presented as to the abstention issue, which was decided by the Ninth Circuit and which is now before this Court, is whether the district courts must wear strait-jackets which preclude them from abstaining when the underlying action is "at law." The stark contrast between the Ninth Circuit's result in *Morgan Stanley*, 18 F.3d 790, and its result in the case below, with the latter result reached *solely* on the basis of the equity/law dichotomy, serves to highlight the unreasonable nature of such a mechanical rule.

In fact, at pages 19 and 20 of its Brief, among other places, Allstate makes clear its own objection to the use of "antique decisions" and "historical distinctions" that "produce arbitrary and anomalous results." Yet Allstate never refutes the fact that the mechanical imposition of the equity/law dichotomy in this case has produced an arbitrary and anomalous result.

Although Allstate now wishes to argue that the district court *should not have abstained*, it never presents a cogent argument to show why the rule should be that the district court *can never abstain* if the underlying case is "at law." The Commissioner proved to the satisfaction of the district court that it had sufficient grounds to warrant abstention and that court was persuaded that unless it abstained it would unduly interfere with the state court insolvency proceedings and the related regulatory scheme.

The question of whether the district court properly exercised its discretion, assuming it had any discretion to abstain in the instant case, is not before this Court. It is relevant to the Commissioner's argument, however, to show that, assuming *arguendo* that the underlying case is properly characterized as being "at law," there can be circumstances in which the principles of judicial federalism and comity serve to compel abstention and that the denial of abstention *solely* on the basis of the equity/law distinction creates an arbitrary and unreasonable result such as that condemned by this Court in *Gulfstream Aerospace Corp. v. Mayacamas Corp.*, 485 U.S. 271 (1988).

D. Allstate's Assertion that the District Court Had No Jurisdiction to Abstain Because Allstate Sought No Injunctive Relief

This new argument, made at pages 30-35 of Allstate's Brief, misses the point. Allstate begins by saying that it "did not bring this lawsuit: the Liquidator did." Allstate's Brief, p. 30. This is correct, but only to a certain extent. It is true that the Commissioner ultimately sued to recover *his* assets and to obtain a declaratory judgment as to the parties' rights under California law as

applied to the reinsurance agreements and the insolvency statutes. But it is also true that Allstate had previously filed its offset claims in the receivership proceedings.

Not only did the Commissioner have the statutory duty to recover the assets of the insurer, which became the receiver's assets by operation of law and by court order, it is *only* the Commissioner, in his official capacity as receiver, who *can* recover them.[14] Moreover, those assets although in the hands of Allstate, were part of the *res* of the receivership proceedings. If the Commissioner took no action, Allstate would end up in permanent possession of receivership assets in derogation of California's insolvency scheme, to the detriment of the policyholders and in violation of California's strong public policy.

Allstate asserts that the maintenance of this one action in federal court will not cause any harm because, among other things, Allstate will only "pursue such defenses as are just and well-founded." While the Commissioner is certainly gratified to have Allstate's assurance that it will only pursue winning defenses, the issue before this Court transcends any such assurances.

If the Ninth Circuit rule stands, it stands for all cases and all insurance insolvency proceedings. The effect of the Ninth Circuit rule is to permit insurers to file claims with receivership courts pursuant to state statutes, but then frustrate the state statutory scheme by removing what constitutes essentially the same claims to a federal court. Whether or not Allstate seeks injunctive relief, the result is a severe and impermissible interference with the state insurance insolvency process—an interference that principles of comity and judicial federalism forbid and that abstention doctrines were created to avoid. Also, Allstate clearly concedes the equitable powers of the federal court in the underlying action when it refers to the relief it is seeking as "either a stay of this litigation . . . or failing that setoff." Allstate's Brief, p. 30. A stay is equitable relief. So is a setoff. Allstate thus admits it *is* seeking

[14] *See* Commissioner's Opening Brief, pp. 10-11, ¶¶ 10-11 nn.26-28.

equitable relief in a case it says is "at law." Yet Allstate then asserts that the relief it requests will not restrain an administrative agency on a matter of peculiarly local concern and therefore the district court had no equitable discretion to exercise. Under the authorities discussed above, this position is both inconsistent and untenable.[15]

California's interest in having an efficient and manageable insolvency process is solidly within its just and vital concern. When Allstate admits it seeks a stay of this process, it admits that it is seeking to interfere with it. The broad prohibition enunciated by the Ninth Circuit would not only permit the kinds of interference the Commissioner faces in the instant case, but would also seem to sanction damage or declaratory judgment actions filed directly in federal court which could not be subject to abstention no matter how much a district court were convinced such a suit interfered with the state court proceedings and the state's insolvency scheme.

E. The Need for a Consolidated Forum

As discussed above, Allstate's assertions that there is no need to have a single insolvency proceeding and to consolidate all actions there is untenable.[16] In addition to

[15] "Moreover, assigning this dispute to the California insurance insolvency court also furthers 'the interstate judicial system's interest in obtaining the most efficient resolution of controversies.'" *Checker Motors Corp. v. Superior Court*, 13 Cal. App. 4th 1007, 1026, 17 Cal. Rptr. 2d 618, 626 (1993) (citing this Court's opinion in *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 292 (1980)). The *Checker* court added, "The entire 'Interstate judicial system' benefits when insurance company involvencies and *all the disputes they generate* can be managed by a single court in a single jurisdiction. . . ." 13 Cal. App. 4th at 1019, 17 Cal. Rptr. 2d at 627.

[16] Allstate attempts to make such of the fact that various orders of the Receivership Court also permit the receiver to pursue actions in other courts. These provisions were included to make it clear that the Commissioner could, in an appropriate case, *choose* to proceed in another court. For example, as Allstate points out, there are provisions for ancillary receiverships in other states which deal with assets in those states. Usually these are limited to certain

being stymied by *United States v. Bank of New York & Trust Co.*, 296 U.S. 463, and the other authorities discussed above, Allstate's argument is also refuted by Cal. Ins. Code § 1058 which provides:

> In any proceeding pending under the provisions of this article, the court in which such proceeding is pending shall have jurisdiction to hear and determine, in such proceeding, all actions or proceedings then pending or thereafter instituted by or against the [insolvent insurer].[17]

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special and statutory deposits required by local law. These are not permitted to interfere with the proceedings in California. *See, e.g., Checker*, 13 Cal. App. 4th 1007, 17 Cal. Rptr. 2d 618, where an effort to use an ancillary proceeding to interfere with the jurisdiction of the California court was flatly rejected. Also, some of the Mission Companies' reinsurers are in *in rem* insolvency proceedings in other states. In appropriate circumstances, it is necessary for the Commissioner to become involved in those proceedings. Further, it might be necessary for the Commissioner to proceed with respect to real estate located in another state. In other instances, the Commissioner has found it necessary to enforce California judgments in foreign countries. There are many reasons why the Commissioner, in the exercise of his discretion might *choose* to go to another court in a limited circumstance. However, as to the core process of marshaling assets and adjudicating claims, the Commissioner needs a single consolidated court.

[17] Allstate cites *Webster v. Superior Court*, 46 Cal. 3d 338, 343-53, 758 P.2d 596, 598-606 (1988) in support of its position that there is no authority for a stay of actions affecting the *res*. However, Allstate misstates the rule in that case. *Webster* was a personal injury case where the injured party sought to recover, not from the insolvent insured, but from its insurer (a third party). Rather than deciding the case as Allstate suggests, the California Supreme Court held that a stay is not mandated by the governing statutes when the claimant makes a binding election not to recover from the insolvent's assets. However, that Court held that if the claimant *does* seek to recover from the insolvent's assets, the action *may* be stayed. Here, Allstate has elected to file its claims seeking to impose a claim on the assets belonging to the Commissioner. Accordingly, *Webster* supports the Commissioner, not Allstate. Further, the California Supreme Court stated that Cal. Ins. Code § 1020 "reflects a legislative intent to preserve an insolvent insurer's assets for orderly disposition by the commissioner." 46 Cal. 3d at 344, 758 P.2d at 599.

Although the sense of the California insolvency statutes is that there will be a single consolidated proceeding in one court, this statute does not expressly provide that the Receivership Court shall have sole and exclusive jurisdiction over all actions and proceedings. However, California Ins. Code § 1020 does explicitly permit the Receivership Court to issue various injunctions and other court orders in order to protect its jurisdiction and the efficacy of the insolvency proceedings. Pursuant to this authority, the Receivership Court in this case, beginning almost 10 years ago, has issued a series of orders which assume sole and exclusive jurisdiction over the assets of the Mission Companies and the exclusive right to hear and determine in the insolvency proceedings all related actions. *See* Commissioner's Opening Brief, pp. 8-9 nn. 19, 20.[18] Under *Underwriters Nat'l Assurance Co. v. North Carolina Life & Acc. & Health Ins. Guar. Ass'n*, 455 U.S. 691, 703-10 (1982), those orders are entitled to respect.

CONCLUSION

For the foregoing reasons and those stated in the Commissioner's Opening Brief, the decision below should be reversed.

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[18] *See Morgan Stanley*, 18 F.3d at 791 where the Ninth Circuit makes the same point.

Respectfully submitted,

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